

Service Date: July 17, 2003

DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA

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IN THE MATTER of NORTHWESTERN)	UTILITY DIVISION
ENERGY'S Application for Electric Supply)	DOCKET NO. D2003.6.77
Deferred Cost Account Balance and Projected)	ORDER NO. 6496a
Electric Supply Cost)	

INTERIM ORDER

Findings Of Fact

1. On June 16, 2003, NorthWestern Energy (NWE) filed its first electric default supply tracker filing with the Public Service Commission (Commission). NWE filed this application late. In Docket No. D2001.10.144, Order No. 6382d, the Commission stated: "A filing for approval of interim rates to recover electricity supply costs for the period July 1, 2003 through June 30, 2004 must be made no later than June 1, 2003." NWE made an allowance for the late filing by requesting that interim rates be effective for service on and after July 15, 2003. The filing contained the following elements: 1) the electric supply deferred cost account balance as of June 30, 2003 and the projected electric supply cost for the twelve month period July 1, 2003 through June 30, 2004, and 2) a request to change the electric cost adjustment from annual to monthly.

2. The primary goal of NWE's proposal to implement monthly filings is to ensure that rates to consumers more immediately reflect the actual market price of electricity, both increases and decreases, therefore providing consumers with accurate price signals. Use of monthly rate changes will help reduce the balance in the electric supply deferred cost account, which will reduce the level of interest on the deferred balance. Monthly electric cost adjustments provide the best match of cash receipts with expenses. The monthly rate change would be based

on annual forecasted electric supply load on a normalized basis for the most recent twelve month forecast.

3. In the June 16th filing, NWE requested approval to reflect the electric supply deferred cost account balance of \$8,178,376 for the twelve month period ending June 30, 2003. This balance includes a cost overcollection of (\$593,935) and \$8,772,311 of under recovery directly attributable to the startup of the new electric tracker. NWE's June 2002 tracker filing included one-half month revenues of authorized rates under the new tracker for service on and after July 1, 2002. NWE's billing system began to reflect these new rates in customer bills on a prorated basis at that time. This means that approximately one-half of the July metered usage, and related revenues, actually covered costs related to power purchased under the "buyback contract" with PPL Montana which expired June 30, 2002. According to NWE these revenues did not cover new default supply costs, and therefore, should not have been included in the tracking period.

4. NWE stated that the 2003 electric default supply tracking filing needs to be processed by the Commission in a timely fashion in order to establish default supply rates that properly reflect the projected costs of default supply resources for the 2003/04 tracking period and recover the 2002/03 deferred account balance.

5. Loads for the 2003/04 tracking period are higher than those in 2002/03 due to the return of a number of choice customers returning to default supply. Customers expected to return to the default supply in the June 16th filing included the League of Cities and Towns and School Board Association, Energy West, Express Pipeline and Cenex. The League of Cities and Towns and the School Board Association are returning to default supply because an affiliate of NorthWestern Energy (NorthWestern Energy Marketing) breached their contract. It appears that this decision to return the League of Cities and Towns and the School Board Association to default supply was made before July 1st. This is demonstrated by these customers being returned to default supply in the June 16th filing. Had the decision been made after July 1, 2003 HB 509, passed by the 2003 Legislation would have applied, with its prohibition against default supply customers being negatively impacted by the return of choice customers.

6. Subsequent information received from NWE indicated that Express Pipeline and Cenex will not return to default supply. Thus, new workpapers were provided by the Company

on July 11, 2003, to reflect the removal of those two customers from the loads presented in the initial filing. Those workpapers will reduce the 546,620 MWh of energy in Finding of Fact No. 7 below.

7. In the June 16th filing NWE indicated that an additional 546,620 MWh of energy would be needed to accommodate the return of former choice loads. Because the existing default supply portfolio is not large enough to serve the additional load, incremental market purchases must be made. The additional market purchases are forecasted to be more expensive than the average cost of NWE's procured resources, increasing the blended commodity rate to default supply customers by approximately \$0.35 per MWh. NWE proposed to offset this increase by approximately \$0.17 per MWh due to the returning choice loads sharing in the cost of the 2002/03 under-collection of \$8.17 million. The proposed net effect to existing default supply customers of the choice loads returning would be an increase of \$0.18 per MWh, or approximately \$900,000 for the 2003/04 tracking year. The cost of service relating to customers returning to default supply will be an issue to be resolved later in this proceeding.

8. The 111 MW unit contingent contract with Duke Energy expired on June 30, 2003. NWE will procure resources to replace the Duke contract as needed, in the short-term market (twelve months and closer). Procured resources from the dispatchable RFP, wind RFP and demand side management activities may not be available as originally projected for the 2003/04 tracker period. The portfolio does maintain a higher degree of risk due to the higher reliance on short-term purchases next year.

9. NWE continually updates and analyzes the hourly, daily, monthly, quarterly, and yearly load forecasts to calculate its net short-term supply requirements. In conjunction with this, NWE closely monitors forward prices to look for opportunities to make forward purchases and/or sales in order to reduce price risk within the portfolio. However, at the time of the June 16th filing, market indications were higher than twelve months ago.

10. The projected unit cost of electricity during the 2003/04 tracking period is \$40.87, an increase of 11 percent over the energy rate in the 2002/03 tracking period.

11. On June 25th the Montana Consumer Counsel issued Data Requests MCC-001 through MCC-022.

12. On July 1st the Montana Consumer Counsel (MCC) filed comments on NWE's application for interim relief in Docket No. D2003.6.77. MCC noted that this filing presents

unique issues for interim rate consideration. This is the case in part due to the proposed recovery of so-called start-up deferred supply cost expense and in part to the lack of precedent and experience with respect to electric default supply. MCC's final position in this Docket may be different from its interim comments.

13. NWE has claimed an under recovery of \$8,772,311 of so-called startup deferred supply cost expense. The Company claims that the startup expense is attributable to a full month of default supply purchase costs in July 2002, but only a half month of default supply revenue. While NWE acknowledges that it did, in fact collect revenue for a full month of service in July 2002, the company argues that due to its metering and billing cycle, one-half of this amount was to pay for June 2002 consumption and one-half for July consumption – with the remaining one-half of July costs being reflected on August bills, and so on. NWE is arguing that energy revenues always lag energy deliveries by half a month, and the Company now proposes to charge ratepayers for the difference. NWE's tracking calculations include only eleven and a half months of revenue, but twelve months of electric default supply expense, even though the purchases are at some point matched with revenues. It appears to MCC that the startup deferred supply cost expense issue is an improper accounting adjustment that should not be included in the electric supply deferred cost account balance. It should be considered, if at all, within the context of the Company's overall working capital needs as part of a proper revenue and cost lead-lag study in a general rate proceeding. This is not an issue that should be dealt with on an interim rate matter.

14. NWE projects that its default supply costs will increase substantially during the next year. This projected increase is due to several primary factors. First, spot market purchases will be a much larger part of the default supply than they have been in the past. This is due to the expiration of the Duke contract without any long-term purchase replacement and to the anticipated return of choice customers to default supply without any corresponding increment to long-term supply. NWE projected substantially higher spot purchase prices during the next year. An increase of 55 percent from \$30.58/MWh in 2002/03 to \$47.54 MWh in 2003/04. Third, the Company has made significant upward revision to a number of its operating cost estimates, including substantially higher costs than previously forecast for transmission and administrative support functions. MCC intends to examine these and other issues, and is not in a position to

judge at this point whether an interim adjustment related to projected costs is necessary to avoid the accumulation of a positive deferred account balance.

15. With respect to the request by NWE for a monthly tracker, MCC indicated that care should be taken to avoid expensive complications to the regulatory process. Monthly adjustments should remain subject to an annual review and approval (or disallowance). It should be recognized that moving to a twelve month rolling average purchased power expense does very little to improve price signals to consumers or to encourage efficient electricity conservation.

16. Due to the Independence Day holiday, NWE will attempt to respond to MCC's first set of Data Requests no later than July 17th. MCC did not object to that timing.

17. On July 3, 2003, NWE sent an email responding to MCC's comments on the interim in the electric default supply tracker. NWE believes that MCC's comments regarding the dilemma a potential bankruptcy poses for customers, potentially leaving customers as unsecured creditors with no recourse for a refund or credit if an interim order were to result in an overcollection, to be well taken. This outcome presents a challenge for the Commission; however, the need for rate levels reflective of actual commodity costs is very real and immediate. NWE cannot operate in the default supplier role if its electric costs do not accurately reflect the costs incurred to buy power in the market for its customers.

18. MCC questioned whether the electric supply deferred cost balance of \$8,178,376 million is truly appropriate for interim treatment. NWE does not challenge the MCC position for interim purposes. NWE combines the startup cost of \$8,772,311 and an overcollection of \$593,935 to reach the net amount of \$8,178,376 million. MCC did not combine the two. MCC's comments went only to the startup cost of \$8,772,311 million being inappropriate for interim purposes. Elimination of the startup costs of \$8,772,311 million for interim purposes is agreed to by the parties and is approved by the Commission.

19. NWE does not challenge MCC's concern about the default supply Administrative Cost on an actual basis (\$1,805,271) being much higher than the 2002/03 forecast (\$769,918). This increase in Administrative Cost is large. The Commission agrees with the parties that this increase in cost needs to be fully reviewed in discovery in this Docket.

20. NWE agrees with MCC's final observation that the use of a monthly adjustment procedure "could address much of the cost projection uncertainties" inherent in this case.

Approval of the monthly tracking proposal will help to ensure that customers will pay accurate prices, and NWE's ability to minimize the deferred balance will be greatly enhanced.

Commission Analysis

Electric Supply Deferred Cost Account Balance:

21. In its June 16th filing NWE for interim proposed an adjustment to remove one half of July 2002 revenues which represented an under collection of \$8,772,311. On July 11, 2003, NWE filed new workpapers which removed that adjustment entirely. The June 16th filing also included an over collection of \$593,935. This over collection was determined for twelve months using estimated information for May and June. Using more current information, NWE has updated this balance to an approximate \$1 million under collection.

22. MCC raised concerns which will be examined later in this case about the increase in the Administrative Cost Account. That account on an actual basis was much larger (234 percent) than the 2002/03 forecast. This issue will be examined by the parties through discovery as this Docket proceeds.

23. Due to these changes since the June 16th filing, NWE proposed and the Commission accepts that the 2002/03 Electric Supply Deferred Cost Account Balance should be set to zero for the purpose of determining interim relief in this Docket.

Default Supply Load Forecast:

24. In its original filing NWE noted that Cenex and Express pipeline would be returning from choice to the default supply. A more recent forecast indicates that both of these customers will remain choice customers. As a result of the updated information the forecast for the next tracking year 2003/04 must be revised to remove these loads from the default supply. This adjustment is approved by the Commission and reduces the amount of power which must be purchased in the short-term market.

Generation from the Milltown Dam:

25. In its June 16th filing there was no power reflected in resources associated with the Milltown Dam. At a regularly scheduled work session on July 10th, the Commission

approved NWE's request to support EWG status for Milltown Dam. As a result of that action it is appropriate to include a normalized power output from Milltown Dam as a part of the resources forecasted for the tracking year 2003/04. This power will be priced at \$32.75 per MWh. This adjustment causes an increase of \$5,323 in transmission costs due to increased off-system sales. The net effect of adding Milltown to the resources in the 2003/04 tracking period is a reduction in the increase contained in NWE's June 16th filing.

Monthly Rolling Average Procedure:

26. NWE requested that a change in the frequency of the electric default supply tracker from annual to monthly. Each month, the new monthly rate would reflect the most recent 12-month forecast of annual supply costs divided by the most recent 12-month forecasted load, plus one-twelfth of the prior 12-month deferred electric account balance. MCC noted that monthly adjustments should remain subject to an annual review and approval (or disallowance). After reviewing this issue the Commission finds that monthly tracking for the electric default supply is in the consumers best interest. The Commission is mindful of the potential volatility of electric prices having just witnessed the crisis in the California energy market in 2000/01. Monthly changes which reflect changes in the cost of electricity will provide more timely price information to consumers and will also help to limit the amount which can build up in the deferred account. The Commission approves NWE's request to change the electric default supply tracker from annual to monthly filings. Use of the rolling average procedure helps to promote both price stability as well as flowing accurate price signals to consumers. The monthly tracker adjustments will be subject to an annual review and approval (or disallowance) by the Commission. Approval of the monthly rolling average mechanism is interim in nature. The Commission may adjust this mechanism in the Final Order in this Docket.

Conclusions of Law

1. NorthWestern Energy provides electric service within the State of Montana and as such is a "public utility" within the meaning of § 69-3-101, MCA.

2. The Montana Public Service Commission properly exercises jurisdiction over NorthWestern Energy's Montana rates, service and operations pursuant to Title 69, Chapter 3, MCA.

3. The Commission may, in its discretion, make temporary approvals of requests pending a hearing or final decision. § 69-3-304, MCA.

4. The rate levels and spread approved in this Order are a reasonable means of providing interim relief to NorthWestern Energy. The rebate provisions of § 69-3-304, MCA, protect ratepayers until there is a final Order in this Docket.

Order

1. NorthWestern Energy shall implement, on an interim basis, rates designed to increase annual jurisdictional electric revenues by \$19,292,361.

2. NorthWestern Energy's request to change the frequency of the electric default supply tracker from annual to monthly is approved by the Commission. This approval is limited to interim treatment at this time. The Commission may adjust the monthly rolling average mechanism in the Final Order in this Docket. The monthly tracker adjustments will be subject to an annual review and approval (or disallowance) by the Commission.

3. NorthWestern Energy shall adhere to and abide by all Findings of Fact in this Interim Order. All rate schedules shall comply with all Commission determinations set forth in this Interim Order.

4. NorthWestern Energy must file tariffs in compliance with the Findings of Fact in this Interim Order.

5. Nothing in this Order precludes the Commission from adopting in its Final Order a revenue requirement different from that contained in this Interim Order.

6. Any interest associated with a refund that may result from the revenue requirement determined in a Final Order in this Docket will be computed at 10.75 percent, the last approved cost of equity approved in Docket No. D2000.8.113, Order No. 6271c.

7. Interim approval of any matters in this proceeding should not be viewed as final endorsement by the Commission of any issues, calculations, or methodologies approved in this Order.

9. This Order is effective for service rendered on and after July 15, 2003.
DONE IN OPEN SESSION at Helena, Montana on this 15th day of July, 2003, by a vote of 5-0.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION

BOB ROWE, Chairman

THOMAS J. SCHNEIDER, Vice Chairman
(voting partial dissent)

MATT BRAINARD, Commissioner

GREG JERGESON, Commissioner

JAY STOVALL, Commissioner

ATTEST:

Barbara J. Effing
Commission Secretary

(SEAL)

NOTE: Any interested party may request the Commission to reconsider this decision. A motion to reconsider must be filed within ten (10) days. See ARM 38.2.4806.